IN THE HIGH COURT OF GUJARAT AT AHMEDABAD

INCOME TAX REFERENCE No. 99 of 1995

For Approval and Signature:

HONOURABLE MR.JUSTICE D.A.MEHTA
HONOURABLE MS.JUSTICE H.N.DEVANI

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1 Whether Reporters of Local Papers may be allowed to see the judgment ?

2 To be referred to the Reporter or not ?

3 Whether their Lordships wish to see the fair copy of the judgment ?

4 Whether this case involves a substantial question of law as to the interpretation of the constitution of India, 1950 or any order made thereunder ?

5 Whether it is to be circulated to the civil judge ?

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COMMISSIONER OF INCOME-TAX - Applicant(s)

Versus

PRABHUDAS KISHORDAS TOBACCO PRODUCTS PVT LTD - Respondent(s)

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Appearance :
MR BB NAIK for Applicant
MR SN SOPARKAR, Sr. Advocate with MRS SWATI SOPARKAR for Respondent
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CORAM : HONOURABLE MR.JUSTICE D.A.MEHTA
and
HONOURABLE MS.JUSTICE H.N.DEVANI

Date : 09/01/2006

ORAL JUDGMENT

(Per : HONOURABLE MR.JUSTICE D.A.MEHTA)

1.The Income Tax Appellate Tribunal, Ahmedabad Bench “C” has referred the following two questions under Section 256(1) of the Income Tax Act, 1961 (the Act) at the instance of Commissioner of Income Tax:

> “[1] Whether the Appellate Tribunal is right in law and on facts in holding that the assessee company is an industrial undertaking for the purposes of Section 80HH and 80I of the I.T Act?
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> [2] Whether the Appellate Tribunal is right in law and on facts in confirming the order made by the CIT (A) whereby he had held the cars, trucks, dead stock, pumps etc. are not plant and machinery for the purpose of determining the cost of project for treating the assessee as small scale industrial undertaking?”

2.The assessment years are 1984-85 and 1985-86 with the relevant accounting periods being years ended on 31st July 1983 and 31st July 1984 respectively. The assessee, a Private Limited Company, claimed relief under Section 80HH and 80I of the Act for both the assessment years. The same was denied by the Assessing Officer on the ground that the activity carried on by the assessee does not constitute an industrial undertaking as required by the provisions. The assessee company was merely buying Tendu-leaves and tobacco, which raw material was thereafter given to contract workers, who in turn roll bidies for the assessee. These bidies were thereafter sold by the assessee company under its brand-name through its sales network. That there has to be some concrete and tangible venture in the path of industry to make it an industrial undertaking. That in case of the assessee, there was absence of an industrial enterprise, there was no industrial activity

and the assessee did not possess any plant and machinery.

2.1 The assessing officer assigned an additional reason for denying relief under Section 80I of the Act. According to him, the assessee was manufacturing goods falling in Entry No.2 of Eleventh Schedule of the Act and hence, unless and until the assessee was a small scale industrial unit, it could not claim the said relief. For the purposes of ascertaining the monetary limit which segregated a small scale industrial unit from an industrial unit, he took into consideration various business assets like cars, trucks, dead-stock, electric fittings, pump and bore etc., to arrive at the total value of the assets at more than Rs.20 lakhs.

3.The assessee carried the matter in appeal before the Commissioner (Appeals) and succeeded. It was held by Commissioner

(Appeals) that the activity carried on by the assessee was a manufacturing activity, namely, manufacturing bidies and thus, the assessee was entitled to relief both under Section 80HH and 80I of the Act. For this purpose, he placed reliance on Allahabad High Court's decision in case of Commissioner of Income Tax, Agra v. Mubarakali Khan, [1980] 123 ITR 101. In relation to the additional reason given by the assessing officer relating to the claim under Section 80-I of the Act, the Commissioner (Appeals) observed that, on one hand, the assessing officer himself had recorded that the assessee did not have any plant and machinery, and on the other hand, for the purposes of determining whether the assessee was a small scale industrial undertaking or not, took into consideration the wide meaning of the word “plant”, which was not justified in view of the definition of “Small Scale Industrial Undertaking” specifically given in Section

80HHA of the Act, which was applicable also for the purposes of Section 80-I of the Act. The Commissioner (Appeals) also took note of the fact that separate balance sheets were drawn for each of the Branches and the total assets were much below the specified limits of Rs.20 lakhs. He also found, as a matter of fact, that there was no plant and machinery in the Branches where the manufacturing of bidies was carried out.

4. Revenue carried the matter in appeal before the Tribunal. However, the Tribunal, for the reasons stated in its order dated 27/8/1992, concurred with the findings recorded by Commissioner (Appeals), to hold that the assessee was entitled to relief both under Section 80HH and Section 80I of the Act. According to Tribunal, the Commissioner (Appeals) had rightly relied upon the decision of the Allahabad High Court in the case of

Commissioner of Income Tax, Agra v. Mubarakali Khan (supra), which directly applied to the facts of the assessee's case. The Tribunal also held that other decisions relied upon by the representative of the assessee supported the case of the assessee.

5. Assailing the aforesaid order of Tribunal, Mr.B.B.Naik, the learned standing counsel for the applicant revenue, submitted that both the Commissioner (Appeals) and the Tribunal had failed to take into consideration that the activity carried on by the assessee was of such a nature that it could not be termed to be a manufacturing activity. According to him, the assessee did nothing on its own, namely, no activity was carried on by the assessee. All that the assessee did was, purchase raw materials to handover the same to outside parties, who in fact rolled the bidies. Thereafter, the assessee merely marketed such

finished products. For this purpose, he invited attention to a decision of this Court in the case of Commissioner of Wealth Tax v. Mohinibai Kanaiyalal, [1999] 240 ITR 636, to submit that the Allahabad High Court's decision, on which reliance had been placed by the Tribunal, had been considered and explained by this Court in the aforesaid decision in case of Commissioner of Wealth Tax v. Mohinibai Kanaiyalal. Even otherwise, according to Mr.Naik, the decision of Allahabad High Court was in relation to claim of exemption under Section 5(1)(xxxii) of the Wealth Tax Act, 1957, and could not be applied for deciding a matter under the Income Tax Act. Last but not the least, a faint attempt was also made to suggest that relief under Section 80HH of the Act is available only to an industrial undertaking, which is set up in a notified backward area. That, in the present case, none of the authorities had recorded any finding in

this regard.

6.Mr.S.N.Soparkar, the learned Senior Advocate, supported the impugned order of Tribunal by placing reliance on the following case-law :

(1)Commissioner of Income Tax v. J.B.Kharwar & Sons, [1987] 163 ITR 394, at page 401 (Gujarat),

(2)Commissioner of Income Tax v. Sidral Food (P) Ltd., [2006] 200 CTR 136 (Gujarat),

(3)M/s Anwarkhan Mahboob Co. v. The State of Bombay (now Maharashtra), AIR 1961 SC 213,

(4)Commissioner of Income Tax v. V.B.Narania & Co., [2001] ITR 884 (Guj.).

It was submitted that, considering the ratio of aforesaid decisions, not only was the assessee company an industrial undertaking, but it was

engaged in an activity which amounted to manufacture i.e. manufacturing of bidies.

7.The tests to ascertain whether an activity amounts to manufacture or production of an article or thing have been laid down and reiterated by various decisions of the Apex Court and this High Court. Broadly, the requirement is: that the raw material must be, in the first instance, subjected to a process of such a nature that it cannot be termed to be the same as the end-product after the raw material undergoes the process of manufacture. In other words, the goods purchased as raw material should go in as inputs in the process of manufacture and the result must be manufacture of other goods. The article produced must be regarded by the trade as a new and distinct article having an identity of its own, an independent market after the commodity is subjected to the process of manufacture.

The nature and extent of the process would vary from case to case, and in a given case, there may be only one stage of processing, while in another case, there may be several stages of processing, and perhaps, a different kind of process at every stage. That with every process, the commodity would experience a change, but ultimately, it is only when the change, or a series of changes, bring about a result so as to produce a new and distinct article, can it be said that the commodity used as raw material has been consumed in the manufacture of the end-product. To put it differently, the final product does not retain the identity of the raw material after it has undergone the process or processes of manufacture.

8. In the case of CIT v. J.B.Kharwar & Sons (supra), this Court was called upon to decide whether the assessee therein was an industrial

undertaking while determining the claim of relief under Section 80J of the Act. It has been laid down at page 401 of the Reports:

> “The question which we have to consider is whether the undertaking of the assessee is an industrial undertaking and whether any articles are manufactured or produced therein. Industrial undertaking has not been defined in the Act. As held by the Supreme Court in Bangalore Water Supply and Sewerage Board v. A Rajappa, AIR 1978 SC 548 : [1978] 52 FJR 197 (SC), the word `industry' has a wide import. It was held that where there is (i) systematic activity, (ii) organized by co-operation between employer and employee (the direct and substantial element is chimerical), (iii)for the production and/or distribution of goods and services calculated to satisfy human wants and wishes

> (not spiritual or religious but inclusive of material things or services geared to celestial bliss, e.g., making on a large scale, prasad or food), prima facie there is an “industry” in that enterprise. It was further observed that the true focus is functional and the decisive test is the nature of the activity with special emphasis on the employer – employee relations. Applying the test laid down by the Supreme Court, it must be held that the activity which is carried on by the assessee is an industry and consequently, its undertaking is an industrial undertaking.”

8.1Whether the assessee carries on the manufacturing activity itself or gets certain processes done from outside, would not make any difference. The said issue is no longer *res integra.* In the case of C.I.T. v. V.B.Narania & Co. (supra), this Court laid down that:

> “The real test for deciding whether the contract is one of employment is to find out whether the agreement is for the personal labour of the person engaged, and if that is so, the contract is one of employment whether the work is time-work or piece-work, or whether the employee did the whole of the work himself or whether he obtained the assistance of other persons also for the work.”

9. Therefore, it is apparent that, applying the aforesaid well established principles, it cannot be said that the assessee company was not an industrial undertaking engaged in business of manufacturing bidies. Tendu leaves and tobacco, which are used as inputs, do not retain independent identity after the bidies are rolled after undergoing several processes. Commercially, the final product is known in the trade as a distinct commodity and has a

separate market for the same. Furthermore, merely because an assessee gets the work done through contract workers, in other words, enters into a contract with the workers and pays them on per piece basis, the relief cannot be denied. The test is whether the outside agency works directly under the supervision and control of the assessee, it being immaterial whether the processing is done by the workers employed by the assessee at a place outside the premises of the assessee. This principle has been laid down by this Court in the case of Commissioner of Wealth Tax v. Mohinibai Kanaiyalal (supra).

10. The Tribunal has, in the circumstances, committed no error when it came to the conclusion that Commissioner (Appeals) was justified in treating the activities carried on by the assessee as amounting to manufacture of bidies, entitling the assessee to reliefs under

Sections 80HH and 80I of the Act.

11.In relation to the additional reason given by the assessing officer for denying relief under Section 80I of the Act, both the Commissioner (Appeals) and the Tribunal have found that, for the purposes of determining whether a unit is a small scale industrial undertaking or not, while ascertaining the monetary limit laid down in the provision, all assets of the business have not to be taken into consideration. This is correct reading of the provision. The Explanation stipulates that an industrial undertaking shall be deemed to be a small scale industrial undertaking if the aggregate value of the machinery and plant installed does not exceed the specified limit. For this purpose, the value that has to be adopted is on the basis of actual cost of plant and machinery which is installed in the industrial undertaking, and used for the purposes of the

business of the undertaking. The provision does not stipulate taking the aggregate value of plant and machinery of the business as a whole, but limits the same to the plant and machinery relatable to the industrial undertaking. Thus, on this count also, there is no infirmity in the view adopted by the Commissioner (Appeals) and the Tribunal concurrently.

12.Accordingly, both the questions are answered in the affirmative i.e. in favour of the assessee and against the revenue.

13.The Reference stands disposed of accordingly. There shall be no order as to costs.

[D.A.MEHTA, J.]

[HARSHA DEVANI, J.]

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